

§ 107.830

STRUCTURING LICENSEE'S FINANCING OF AN ELIGIBLE SMALL BUSINESS: TERMS AND CONDITIONS OF FINANCING

§ 107.830 Minimum duration/term of financing.

(a) *General rule for Section 301(c) Licensees.* If you are a Section 301(c) Licensee, the duration/term of all your Financings must be for a minimum period of five years. *Exception:* You may finance a Disadvantaged Business for a minimum term of four years.

(b) *General rule for Section 301(d) Licensees.* The duration/term of your Financings may be for a minimum period of four years.

(c) *Restrictions on mandatory redemption of Equity Securities.* If you have acquired Equity Securities, options or warrants on terms that include redemption by the Small Business, you must not require redemption by the Small Business within the first five years of your acquisition except as permitted in § 107.850.

(d) *Special rules for Loans and Debt Securities.* (1) *Term.* The minimum term for Loans and Debt Securities starts with the first disbursement of the Financing.

(2) *Prepayment before five years.* You must permit voluntary prepayment of Loans and Debt Securities by the Small Business at any time during the initial five year term. You must obtain SBA's prior written approval of any restrictions on the ability of the Small Business to prepay other than the imposition of a reasonable prepayment penalty under paragraph (d)(3) of this section.

(3) *Prepayment penalties.* You may charge a reasonable prepayment penalty which must be agreed upon at the time of the Financing. If SBA determines that a prepayment penalty is unreasonable, you must refund the entire penalty to the Small Business. A prepayment penalty equal to 5 percent of the outstanding balance during the first year of any Financing, declining by one percentage point per year through the fifth year, is considered reasonable.

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§ 107.835 Exceptions to minimum duration/term of Financing.

You may make a Short-term Financing for a term less than five years if the Financing is:

(a) An interim financing (for a period not to exceed one year) in contemplation of long-term Financing. The contemplated long-term Financing must be in an amount at least equal to the short-term Financing, and must be made by you alone or in participation with other investors; or

(b) For protection of your prior investment(s); or

(c) For the purpose of Financing a change of ownership under § 107.750. The total amount of such Financings may not exceed 20 percent of your Loans and Investments (at cost) at the end of any fiscal year; or

(d) For the purpose of aiding a Small Business in performing a contract awarded under a Federal, State, or local government set-aside program for "minority" or "disadvantaged" contractors.

§ 107.840 Maximum term of Financing.

The maximum term of any Loan or Debt Security Financing must be no longer than 20 years.

§ 107.845 Maximum rate of amortization on Loans and Debt Securities.

The principal of any Loan (or the loan portion of a Debt Security) with a term of five years or less cannot be amortized faster than straight line. If the term is greater than five years, the principal cannot be amortized faster than straight line for the first five years.

§ 107.850 Restrictions on redemption of Equity Securities.

(a) A Portfolio Concern cannot be required to redeem Equity Securities earlier than five years from the date of the first closing unless:

(1) The concern makes a public offering, or has a change of management or control, or files for protection under the provisions of the Bankruptcy Code, or materially breaches your Financing agreement; or

(2) You make a follow-on investment, in which case the new securities may be redeemed in less than five years, but no earlier than the redemption date associated with your earliest Financing of the concern.

(b) The redemption price must be either:

(1) A fixed amount that is no higher than the price you paid for the securities; or

(2) An amount that cannot be fixed or determined before the time of redemption. In this case, the redemption price must be based on:

(i) A reasonable formula that reflects the performance of the concern (such as one based on earnings or book value); or

(ii) The fair market value of the concern at the time of redemption, as determined by a professional appraisal performed under an agreement acceptable to both parties.

(c) Any method for determining the redemption price must be agreed upon no later than the date of the first (or only) closing of the Financing.

§ 107.855 Interest rate ceiling and limitations on fees charged to Small Businesses ("Cost of Money").

"Cost of Money" means the interest and other consideration that you receive from a Small Business. Subject to lower ceilings prescribed by local law, the Cost of Money to the Small Business must not exceed the ceiling determined under this section.

(a) *Financings to which the Cost of Money rules apply.* This section applies to all Loans and Debt Securities. As required by § 107.800(b), you must include as Debt Securities any equity interests with redemption provisions that do not meet the restrictions in § 107.850.

(b) *When to determine the Cost of Money ceiling for a Financing.* You may determine your Cost of Money ceiling for a particular Financing as of the date you issue a Commitment or as of the date of the first closing of the Financing. Once determined, the Cost of Money ceiling remains fixed for the duration of the Financing.

(c) *How to determine the Cost of Money ceiling for a Financing.* At a minimum, you may use a Cost of Money ceiling of 19 percent for a Loan and 14 percent for

a Debt Security. To determine whether you may charge more, do the following:

(1) Choose a base rate for your Cost of Money computation. The base rate may be either the Debenture Rate currently in effect or your own "Cost of Capital" as determined under paragraph (d) of this section.

(2) For a Loan, add 11 percentage points to the base rate; for a Debt Security, add 6 percentage points. In either case, round the sum down to the nearest eighth of one percent.

(3) If the result is more than 19 percent (for a Loan) or 14 percent (for a Debt Security), you may use it as your Cost of Money ceiling.

(4) If two or more Licensees participate in the same Financing of a Small Business, the base rate used in this paragraph (c) is the highest of the following:

(i) The current Debenture rate;

(ii) The Cost of Capital of the lead Licensee; or

(iii) The weighted average of the Cost of Capital for all Licensees participating in the Financing.

(d) *How to determine your Cost of Capital.* "Cost of Capital" is an optional computation of the weighted average interest rate you pay on your "qualified borrowings". "Qualified borrowings" means your Debentures together with your borrowings at or below the usual interest rate charged by banks in your locality on the date your loan was made.

(1) For any fiscal year, you may compute your Cost of Capital:

(i) As of the first day of your fiscal year, to remain in effect for the entire year; or

(ii) As of the first day of every fiscal quarter during the fiscal year, to remain in effect for the duration of the quarter.

(2) For each qualified borrowing outstanding at your last fiscal year or fiscal quarter end, multiply the ending principal balance (net of related unamortized fees) by the number of days during the past four fiscal quarters that the borrowing was outstanding, and divide the result by 365.

(3) Add together the amounts computed for all borrowings under paragraph (d)(2) of this section. The result is your weighted average borrowings.